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Rebuilding the U.S. Merchant Marine

BY CLARENCE N. WEEMS, Jr.

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with the aid of the Research Staff of the Foreign Policy Association

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THE candid report issued by the Maritime Commission in November has once more focused attention on our merchant marine policy. By frankly exposing the deplorable condition of American shipping, it has placed two issues squarely before Congress and the public. The question of government versus private ownership must be resolved before long; and the American people must decide whether they will make the necessary financial sacrifices to insure a satisfactory, if belated, rejuvenation of the merchant marine.

As recently as June 1936, Congress passed a new Merchant Marine Act—the third major shipping law enacted in the United States since the World War. Like its predecessors—the Merchant Marine Acts of 1920 and 1928—this legislation seeks to foster a strong and efficient American merchant marine, capable of meeting the nation's commercial and naval auxiliary shipping needs. Like them, also, it deals with many problems having their roots in the abnormal expansion of American tonnage which was effected during the World War under authority of the Shipping Act of 1916.

From this country's 20-year experiment in large-scale shipping has emerged the fairly definite concept that American operators labor under certain permanent and inevitable competitive handicaps imposed by relatively high standards of living. In a shamefaced and faltering manner previous measures—and more particularly the Act of 1928—have poured millions of dollars into private American shipping and shipbuilding industries in a disguised effort to overcome these handicaps. Despite some noteworthy improvements, the merchant fleet has not been fundamentally transformed under government stimulation, and today is largely unfit for successful commercial competition or for national defense. Its efficiency has been further threatened by protracted labor difficulties, while its safety has been called in question by several spectacular maritime disasters.

At the outbreak of the World War the American merchant marine was negligible as an instrument of national commerce or of national defense.[1] For all practical purposes, the existing shipping problems may therefore be regarded as the result of developments during the past twenty years.

The Act of 1916 was inspired in part by a desire to build a naval auxiliary fleet to guard against the possibility of this country's involvement in the World War. A motive which was pressed even more actively by its proponents was that of providing shipping facilities to relieve American commerce from dependence on foreign bottoms, not only under war conditions but also in time of peace. To accomplish both these objectives, the Act set up a Shipping Board with power to build and buy ships and with important regulatory functions which will be reviewed in the light of their direct bearing on the Act of 1936.

Whatever may have been the intention of framers of the Shipping Act, this effort to build a government fleet came to be regarded after the war as an emergency measure for which the occasion had passed, and subsequent legislation was directed toward the creation of a privately owned merchant marine with government aid. In at least two important respects, the conditions under which this new program was undertaken were traceable to this country's participation in hostilities overseas. First, the war emergency had retarded the allocation of new vessels to commercial routes which had been a major objective of the Shipping Act. It was thus necessary to make almost a completely new effort to strengthen the hold of the United States on the peace time carrying trade.

1. As of June 30, 1914 there were only 116 American-flag vessels (626,848 gross tons) employed in trade with all foreign countries and with United States possessions; as of January 1, 1936 there were 538 vessels (3,192,335 gross tons) so employed. *Report No. 1500-7-A*, United States Maritime Commission, Division of Research, as of January 1, 1936. In the years immediately preceding the war, about 10 per cent of this country's foreign commerce was carried in American bottoms, as contrasted with about 35 per cent since 1923.

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Secondly, the Shipping Board's building program of 1917-1922 hastily produced a vast fleet of uneven quality. Some of these vessels were as much as five years old in design when completed, many were structurally unfit for any sustained service, and most of them were necessarily built without relation to the volume or character of tonnage required for an evolutionary expansion of American-flag services. Fortunately, some have in fact been reasonably efficient in certain routes.

For the double purpose of liquidating this government-owned fleet and of strengthening American-flag services, the Acts of 1920 and 1928 extended three forms of financial aid to private operators. One of these was the sale of government ships at greatly reduced prices in return for engagements to operate them on specified routes considered by the Shipping Board essential to the nation's commerce. Another was the establishment of the Construction Loan Fund—$250,000,000—from which American operators might obtain 20-year loans to the extent of 75 per cent of the cost of approved new construction or reconstruction of existing vessels at interest rates varying from one-eighth of one per cent to 3½ per cent.[2] The third and most ambitious form of aid was embodied in the system of mail contracts, for which the Act of 1928 provided on a large scale. Under this Act many shipping companies received 20-year contracts which entitled them to substantial subsidies, based on mileage rates, for maintaining designated services and for replacing and rebuilding certain of their vessels.[3]

FAILURE OF SUBSIDY PROGRAM

Discounts on the 220 Board-owned vessels sold into designated services totaled approximately $24,000,000. The differential between the interest actually paid on CLF loans and the sums which would have been paid at a commercial rate of 5 per cent is estimated at $45,000,000. Mail contract payments in excess of those ordinarily paid American ships for carrying mail amounted to about $176,000,000 by June 30, 1937. Over and above the stupendous outlays made to build a fleet at war prices and to cover operating deficits on the vessels which were retained by the Shipping Board,[4] the government has thus spent about $245,000,000 under the two post-war Acts preceding the law of 1936 to sponsor a privately owned merchant marine.[5]

An appraisal of the value received for this expenditure must be based on a comparative analysis of the American commercial fleet of today. On December 31, 1936 the fleets of the eight principal maritime nations normally available for carrying passengers and general cargo in foreign trade stood in the following order:

FOREIGN TRADE FLEETS OF LEADING SHIPPING COUNTRIES

	TOTAL GROSS TONNAGE		GROSS TONNAGE OF VESSELS 12 KNOTS AND OVER		GROSS TONNAGE OF VESSELS 10 YEARS OF AGE AND UNDER	
Nationality	*Gross Tons*	*Percentage*	*Gross Tons*	*Percentage*	*Gross Tons*	*Percentage*
British Empire	13,099,000	44.67	8,287,000	47.46	4,689,000	55.32
Japan	3,059,000	10.43	1,614,000	9.24	774,000	9.13
United States	2,685,000	9.16	1,363,000	7.81	416,000	4.91
Germany	2,813,000	9.59	2,015,000	11.54	1,020,000	12.03
Italy	2,283,000	7.79	1,242,000	7.11	418,000	4.93
France	2,177,000	7.43	1,521,000	8.71	528,000	6.23
Netherlands	1,653,000	5.64	1,265,000	7.25	579,000	6.83
Greece	1,552,000	5.29	153,000	0.88	52,000	0.62
Total	29,321,000	100.00	17,460,000	100.00	8,476,000	100.00

Vessels of less than 2,000 gross tons are not included.
Source: Signed Memorandum from Division of Research, United States Maritime Commission, August 17, 1937.

The United States is fourth in foreign trade tonnage and fifth in respect to the speed of ships. In modern tonnage in operation, it actually ranks eighth, since Norway, which is not included in the table because its total tonnage is slightly less than that of Greece, had 587,000 gross tons of vessels

2. Under the 1920 Act as amended in 1922, the minimum interest rate was 4¼ per cent and the amount of the loan was limited to 66⅔ per cent of the vessel's value.

3. Cf. John C. deWilde, "Ship Subsidies and the Future of World Shipping," *Foreign Policy Reports,* March 14, 1934.

4. The total cost of the American merchant marine to the government for the period 1917 to 1937 inclusive was no less than $3,575,736,398 of which over $3,000,000,000 was spent during and immediately after the war for the construction of about 2,500 vessels. Cf. United States Maritime Commission, *Economic Survey of the American Merchant Marine,* November 10, 1937, pp. 78-79.

5. These figures are based on the results of the Postmaster General's investigations in 1934, and on data from the Post Office Department and the Shipping Board Bureau covering the intervening period. *Report of the Postmaster General to the President on Hearings Conducted by the Post Office Department on Foreign Air-Mail Contracts and Ocean-Mail Contracts,* January 11, 1935, Part 1, pp. 3-8; *Report No. 1105,* Division of Shipping Research, U.S. Shipping Board Bureau, August 31, 1935; Signed memorandum from the Division of International Postal Service, Post Office Department, February 18, 1937.

ten years of age or less at the beginning of 1936.[6] Not a single cargo ship has been built in the United States for the foreign trade since 1922, and no passenger-carrying vessels have been built for the foreign trade in the past four years.[7] Eighty-eight per cent of the number and 83 per cent of the gross tonnage of our foreign trade vessels will be obsolete (over 20 years old) by 1942 and, of these, 61 ships (401,000 tons) are already over-age.[8]

The speed and modernity of vessels of each category in the entire American ocean-going fleet are also matters of interest, especially in connection with a national defense program. In tankers, American operators are well supplied with tonnage which is satisfactory for commercial service but, because of its low speed, is of negligible value for naval purposes.[9] Most of the tonnage built in this country since 1922 has consisted of combination passenger and cargo vessels, and in this category the position of the combined American domestic and foreign trade fleets is comparatively strong.[10] The trend in the percentage of the world's large fast liners flying the American flag has, however, been downward in the last four years.[11]

The greatest deficiency of the whole American ocean-going fleet is in general cargo vessels. While this country owns 20 per cent of the world's tonnage in this category, it has only 7½ per cent of the cargo tonnage capable of 14 knots or more, and less than one per cent of the cargo tonnage built within the last ten years.[12]

Already handicapped by the approaching obsolescence of much of its tonnage, the American merchant fleet has suffered further from the loss of public confidence caused by the much-publicized marine disasters involving the Ward liners *Morro Castle* and *Mohawk*. In actual fact, the loss of 355 lives in the fiscal year 1935 was highly abnormal, for the record reveals that the United States has made greater progress than any other country in reducing the percentage of the merchant fleet lost from year to year.[13] To restore confidence, Congress in 1935-1937 enacted more legislation to improve human and mechanical factors in sea safety than in the last quarter of a century.[14]

Although government aid has been instrumental in building up a number of American shipping services, and forty-two new passenger and cargo vessels were constructed under the provisions of the 1928 Act, our post-war ship-subsidy program has on the whole failed in its purpose of creating and maintaining a modern, efficient merchant marine. The Shipping Board has had to struggle with a large fleet of vessels all built at extremely high war-time costs, many of which were ill-suited for operation on commercial lines under conditions of keen competition. No real attempt was made to develop a replacement program until the 1928 Act, and then lax administration and the advent of the depression prevented building on an adequate scale. Moreover, there was no attempt to segregate funds for construction aid from those intended for assistance in the continuous burden of operation, nor was there any effective scientific means for determining the actual cost differentials faced by a given operator. The principle of competitive bidding, which might theoretically have served to determine the minimum subsidy covering actual cost handicaps, was not in fact a desirable basis for awarding contracts, since the operator already serving the route to be covered by the contract was in almost all cases the sole possible bidder.

6. Memorandum prepared by Division of Shipping Research, U.S. Shipping Board Bureau, May 13, 1936. Cf. remarks by Joseph P. Kennedy, chairman, U.S. Maritime Commission, *Journal of Commerce*, August 17, 1937.

7. Shipping Board Bureau Memorandum, cited. Cf. also Maritime Commission Memorandum of August 17, 1937, cited.

8. *Economic Survey of the American Merchant Marine*, cited, p. 38.

9. Cf. testimony of Alfred H. Haag, *Hearings before the Committee on Commerce, United States Senate, Seventy-fourth Congress, Second Session, on S. 3500* (Copeland Bill), *S. 4110* (Guffey Bill), and *S. 4111* (Gibson Bill), March 9 and 10, 1936 (hereinafter cited as *Copeland Committee Hearings, 1936*), p. 245. As of June 30, 1936, the British Empire, the United States, and Norway had 31.22, 30 and 20.35 per cent, respectively, of the ocean-going tanker vessels of 2,000 gross tons or more owned by the eight leading nations. In vessels with speeds of 12 knots or more, the respective percentages were: 29.81, 9.92 and 35.9, and in vessels ten years old or less, the percentages were 34.41, 8.21 and 34.15. Computed from statistics in *Report No. 1100*, U.S. Shipping Board Bureau, Department of Commerce, June 30, 1936.

10. Cf. *ibid.* Of the world's ocean-going combination vessels of 2,000 gross tons or more owned by the eight leading nations on June 30, 1936, the United States had 14.6 per cent of the total tonnage, 25.06 per cent of the vessels capable of 18 to 20 knots and over, and 13.24 per cent of the ships ten years of age and less. In speed and tonnage it ranked second to the British Empire, but both the German and British fleets were more modern.

11. The United States and Italy were the only leading nations which failed to build any combination vessels from January 1, 1934 through June 30, 1936. In this 2½-year period the British Empire built 21 such vessels; Japan 8; Germany 7; France 4; the Netherlands 2; and Spain 2.

12. Cf. *Report No. 1100*, cited.

13. *Lloyd's Register of Shipping*, quoted in *National Council of American Shipbuilders, Annual Report, April 1, 1937*, Appendix, Table 16. In 1935 the United States ranked second to the Netherlands in safety records as expressed by percentage of losses at sea in comparison with total tonnage.

14. Especially important are: 1929 International Convention for Safety of Life at Sea (ratification); Coastwise Load Line Act (Public No. 720); Motorship Act (Public No. 722); Automatic Sprinklers Act (Public No. 712); Model Basin Act (Public No. 568); Dangerous Cargo Act (Public No. 765); Act for the Reorganization of the Bureau of Marine Inspection and Navigation (Public No. 622); and the Copeland Personnel Act (Public No. 808); all passed by the 74th Congress. The Copeland Ship Radio Act (Public No. 97), passed by the 75th Congress, has continued this legislative program.

In addition, the machinery set up for the administration of shipping aid was sadly deficient.

The unfortunate results of this system are already well known. Subsidies were, in practice, granted at the same rates to almost all contractors —that is, at the maximum allowable rates—and were thus in no way accommodated to the varying conditions and cost handicaps found in different services. In many cases obviously inadequate replacement requirements were incorporated in the mail contracts at the insistence of influential contractors. Subsidy funds which should have built vessels or created reserves were diverted to innumerable other purposes. Another—and fatal—consequence was the failure to maintain a marine personnel of ability, loyalty, and reasonable economic security and contentment. Responsibility for these abuses must be attributed in part to private shipping interests, and in part to government officials who "opened the gates" to the subsidy treasury. But the original cause can be found in the terms of the 1920 and 1928 Acts.

THE MERCHANT MARINE ACT OF 1936

To remedy these defects, Congress passed the Merchant Marine Act of 1936. This Act abandons the subterfuge of mail contracts and provides direct subsidies to meet the difference between foreign and American costs of constructing and operating vessels. By clearly separating construction aid from operating aid, the Act proposes both to simplify the task of determining existing differentials and to prevent the haphazard use of government funds which had been possible under the Act of 1928. It seeks to prevent the diversion of subsidy funds from their intended purposes by specifically prohibiting recipients of operating aid from having any financial interest in the various types of enterprises most frequently used to "pipe" away mail contract funds. In order to avoid confusion and irresponsibility in administration, the law vests all administrative power in a single commission. Finally, it makes some effort to standardize and improve maritime labor personnel.

The Act creates a Maritime Commission of five members, each of whose tenure will ultimately be six years. This body functions as (1) a regulatory arm of the Federal government; (2) a policy-making and promotional organization; (3) a government-owned shipping concern; and (4) the sole agency for the determination, payment and supervision of shipping and shipbuilding subsidies.

As a regulatory body, the Commission has been assigned all powers and duties vested in the Shipping Board by extant portions of the Acts of 1916, 1920 and 1928,[15] and the Intercoastal Shipping Act of 1933. In general, such of these provisions as were regulatory in nature empowered the Board to pass upon the fairness of all agreements between two or more common carriers; to prescribe maximum rates if necessary; and to prevent discriminatory and retaliatory practices such as the use of "fighting ships," deferred rebates and speculative fluctuations of rates. The President is authorized, however, to transfer these particular functions to the Interstate Commerce Commission after the expiration of two years from October 26, 1936—the effective date of the Act.

As a policy-making and promotional organization, the Commission is directed to determine those lines which are essential to American commerce and to make definitive studies of many other economic, technological and administrative questions[16] besides those required in fixing the differential subsidies later to be discussed.

On the basis of these studies and a physical appraisal of the present fleet, the Commission is required to prepare and adopt a "long-range program for replacements and additions to the American merchant marine." It is to prepare its specifications in close collaboration with the Navy Department and with special emphasis on insuring maximum safety. Moreover, its studies are to serve as the basis for certain active promotional work.

15. Many of the provisions of the Acts of 1916 and 1920, as well as virtually all the significant ones of the 1928 Act, were repealed by the 1936 Act (Section 903). A useful summary of the present status of each of these laws is found in John Nicolson, *The Maritime Subsidies under Titles V and VI of the Merchant Marine Act, 1936, including relevant provisions of other portions of that Act; also of the Shipping Act, 1916; and of the Merchant Marine Act, 1920, with Analytic and Expository Comments* (New York, 1937), pp. 243-46.

16. The Commission's most fundamental assignment in the economic field is directly connected with its designation of "essential" routes, and consists of drawing up a plan showing the precise complement of American-flag vessels which it considers each foreign trade route should have to serve the potential as well as actual volume of American commerce over that route (Section 211,a). It is to specify types of vessels and frequency of sailings, and to consider particularly the advantages of super-liner vessels (Section 211,b). A special topic (Section 211,h) is the possible desirability of governmental assistance to reduce freight rates on outward cargoes of general farm products, cotton, coal, lumber and cement during business depressions which make it difficult for growers and producers to transport these commodities to foreign markets. The Commission is directed to make special recommendations to Congress with regard to the scrapping of obsolete tonnage, both publicly and privately owned (Section 213,a), and the advisability of encouraging American operators to engage in tramp service (Section 213,b). Provision is made for technological research to develop plans for merchant vessels which will take advantage of the latest advances in the technique of propulsion and will take into consideration the desirability and feasibility of standardized production (Sections 211,i and 212,c). An administrative problem on which the Commission must make a prompt report to Congress is that between construction cost differences on the different sea-coasts and equitable means of overcoming them (Section 213,c).

It is directed "to cooperate with vessel owners in devising means by which . . . there may be constructed . . . express-liner or super-liner vessels comparable with those of other nations." It is also charged to cooperate with ship-owners, private trade organizations and all interested agencies of the Federal government in a planned effort to increase the percentage of this country's import and export trade carried in American bottoms.

The Maritime Commission took over from the Shipping Board on October 26, 1936 a fleet of 242 old vessels, appraised at $17,764,615, and seven shipping services operated for the government by private contractors. Its total assets, including cash and accounts receivable, aggregated $221,208,506.[17] While the Commission is not now an important ship-owner, its opportunity to accumulate a new government-owned merchant marine is virtually unlimited under Title VII of the 1936 Act. Whenever the Commission, with the concurrence of the President, decides that private enterprise, aided by differential subsidies, is not proceeding satisfactorily with execution of the merchant marine program outlined by the Commission itself, it may have vessels built for its own account. These ships may be built by the private American shipbuilder submitting the lowest responsible bid, but the Commission is empowered to reject all bids and resort to construction in United States navy yards. Any vessels constructed under Title VII are to be employed exclusively in the foreign trade. They are ordinarily to be let out on bare-boat charter[18] for operation on specified routes, on the basis of competitive bids. Whenever the Commission finds, however, that an "essential" route cannot be developed and served by any private operator without additional aid beyond the differential subsidies, it may charter its vessels to the American operator already established in that trade, without competitive bidding, at an annual hire of 5 per cent of their construction cost.

Administration of the subsidy system set up by the Act is the most immediate task of the Commission, and the one involving the most important consequences for the whole future of American shipping. Under the subsidy provisions the Commission is, first of all, a fact-finding body with legislative powers. It will not only accumulate data on differentials in construction and operation costs and on maritime labor conditions, but will also act as sole judge of the correctness of its own conclusions and will fix subsidies and working conditions in accordance with these findings. Secondly, the Commission is a board of examiners with final authority to determine the economic need for a subsidy in any given case and the qualifications of the particular applicant concerned. Thirdly, it is the custodian and disbursing agent for subsidy funds, subject only to auditing by the General Accounting Office. Finally, it is also the agency for enforcing the innumerable financial, commercial and sociological requirements and restrictions to be incorporated in the new subsidy contracts.

THE DIFFERENTIAL SUBSIDY SYSTEM

The Act liquidates the Construction Loan Fund and transfers sums remaining in it to the Commission. It requires the termination of all mail contracts made under the Act of 1928 by the end of the fiscal year 1937 and charges the Commission to make equitable settlements with contractors. The Postmaster General's authority to execute any more such contracts is revoked, but the 1936 Act stipulates that the transportation of United States mails at poundage rates[19] must be performed by American-flag vessels whenever practicable. To replace both the loan fund and the mail contracts, the Act provides separate grants for construction and for operating purposes which it frankly calls subsidies.

The amount of the construction differential subsidy to be allowed an American operator for a given vessel will be determined by the difference between the lowest responsible bid submitted by an American shipbuilder and the "fair and reasonable estimate of cost, as determined by the Commission," which this operator's principal foreign competitors would actually incur for a ship of identical specifications. This estimate is to be based on costs prevailing in "a principal foreign shipbuilding center" which is ordinarily patronized by the particular foreign competitors concerned and which also affords a "fair and representative example" of the cost of such a ship in foreign countries generally.[20] The allowable "differential" is

17. United States Maritime Commission, *Report to Congress for the Period of October 26 to December 31, 1936* (Washington, Government Printing Office, 1937), p. 8.

18. A bare-boat charter is a lease which obliges the charterer to pay all voyage and cargo expenses and to engage and compensate the officers and crew.

19. The Postmaster General's authority to prescribe poundage rates for mail carriage by American-flag vessels is independent of the Universal Postal Union Conventions, but in practice the new rates which he established in 1936 correspond with the international rates prescribed by the Convention now in force. Signed Memorandum from Division of International Postal Service, Post Office Department, January 22, 1937.

20. Nicolson (*The Maritime Subsidies*, etc., cited, p. 32) remarks: "It is not apparent why the intermediate test-market need be introduced. To select a foreign yard or 'center' as an exponent of the rates prevailing in foreign countries generally, it is obvious that the Commission must first have ascertained the rate prevailing in foreign countries generally—and *that* is

ordinarily to be limited to 33⅓ per cent of the American cost of the vessel, but if the Commission finds "conclusive evidence that the actual differential is greater," it may extend the subsidy to 50 per cent of the American cost. Conspicuous by its absence is any blanket authority on the part of the Commission to grant still further construction aid to offset foreign construction bounties.

The mechanics of paying the subsidy are designed to enforce the complete segregation of construction aid from that for operating purposes and to preclude collusion between the builder and the prospective owner of a vessel. The operator submits specifications for a new ship to be built with subsidy assistance and to be operated in his particular trade route. If the Commission approves the proposal, it will obtain the Navy Department's detailed recommendations regarding special features to be built into the vessel in preparation for naval auxiliary service. The Commission may then invite sealed bids from American shipbuilders for the construction of the vessel for its own account. It may have the vessel built by the lowest responsible bidder[21] or, if all bids appear "collusive, excessive or unreasonable," it may have the vessel built in a navy yard, provided, in either case, that the applicant operator has contracted to buy it from the Commission on completion. The applicant's contract will bind him to pay the cost of the ship (exclusive of the cost of national defense features) to the Commission, less the differential determined by that body. This subtraction of the differential is intended to make the price to be paid by the applicant equal to the foreign cost. He must make a down payment equivalent to 25 per cent of the actual cost of the vessel paid by the Commission, but an obsolete vessel owned by the applicant may be accepted by the Commission as partial consideration for this down payment, provided the old vessel has been operated in the foreign trade under the American flag for ten years. The difference between the down payment and the total purchase price will become a 20-year, 3½ per cent obligation of the applicant to the United States. The new vessel must be operated in foreign trade and must retain its American registry for twenty years even if all purchase notes are paid before the expiration of that time.

Contract relations between the Commission and any private shipbuilder constructing a vessel for its account are defined in detail. The outstanding features are the provisions which permit the recapture of all net profits in excess of 10 per cent made on Commission contracts[22] and which limit the size of any individual's salary allowable as an item of construction cost to $25,000 a year.

The operating-differential subsidy[22a] is designed to meet two distinct handicaps facing the American-flag operator of an "essential" service—first, the actual excess of his day-to-day operating expenses[23] over those incurred by foreign competitors; and, secondly, the enjoyment by those competitors of financial aid from their governments. Equalization of the first form of differential will be a normal and regular function of the Commission for "essential route" vessels meeting specified conditions,[24] but a "subsidy to meet subsidy" will constitute an extraordinary grant, requiring the unanimous approval of the Commissioners.

The Commission's subsidy contract with respect to a given ship or fleet may run for twenty years.[25] Of the requirements to be fulfilled by the contractor, four are most fundamental. First, he must observe minimum scales of wages and manning prescribed by the Commission. Secondly, he cannot remove the vessel from one particular route so long as the operating subsidy continues. Thirdly, at the end of each 5-year period he must return to the Commission one-half of any net profits (after deduction of depreciation charges) in excess of 10 per cent on his capital investment.

the ultimate information which it wants; whether some one particular foreign yard or 'center' is an exponent of such composite rate is not material."

21. In the case of a vessel to be built for a Pacific Coast operator, the Commission is required to accept the lowest responsible bid of a Pacific Coast shipbuilder if it is not more than 6 per cent in excess of the lowest responsible bid submitted by any Atlantic Coast builder (Section 502,d).

22. The Commission has final authority to judge the amount of such profits, except that it has no choice with respect to the salary limitation mentioned. It may determine whether the contractor's itemization of construction costs is "fair, just and not in excess of a reasonable market price for commodities or goods or services." The Commission is entitled to free access to the contractor's premises and records for inspection and auditing.

22a. Under the 1936 Act no subsidies may be granted to ships engaged partly in coastwise or intercoastal trade. The resulting loss of mail subsidies was one factor prompting the Grace Lines and Panama Pacific Line to give up their services between the Atlantic and Pacific coasts of the United States. Cf. *New York Times*, November 14, 1937.

23. The Act (Section 603,b) defines these expenses as follows: "insurance, maintenance, repairs not compensated by insurance, wages and subsistence of officers and crews, and any other items of expense in which . . . the applicant is at a substantial disadvantage in competition."

24. Any vessel to be subsidized must be not more than twenty years of age (Section 605,b), must be a steam or motor ship of metal construction (Section 610), must have been built in the United States or documented under its laws not later than February 1, 1928 (Section 610), and must have approved naval auxiliary features if built after passage of the Act (Section 610). The applicant must, of course, satisfy the Commission as to his ability and reliability.

25. Subsidy payments will be reduced, however, for any portions of the 20-year period in which the vessel is laid up (Section 606) and proportionately reduced for domestic portions of a route serving more than one American port as well as foreign ports (Section 605,a).

Finally, he may not pay to himself or to any employee an annual salary of more than $25,000.

The Act proposes to close off the favorite "pipes" for diverting subsidy funds by prohibiting a holder of an operating subsidy contract or a charterer of Commission-owned vessels from having financial interest in ship-servicing operations,[26] domestic trade operations, or foreign-flag operations.[27] It also seeks to prevent lobbying by requiring expense records from contractors and their subsidiaries. The Commission is directed to require all operating contractors and charterers to keep uniform records, which are to be scrupulously audited; it may subpoena persons and records for any investigation it undertakes.

INCREASING FOREIGN SUBSIDIES

The volume of American marine subsidies will necessarily be governed to a large extent by the assistance given by other countries to shipping, and any retaliatory subsidies granted by competing nations will to some degree affect the success of the new American program. Recent developments apparently demonstrate that, despite strong disapproval in principle on the part of a few maritime countries, almost all of them are pursuing increasingly nationalist shipping policies and are prepared to pay vast subsidies to foster and maintain their own merchant marines. Of the major shipping powers, only the Netherlands and the Scandinavian countries have managed to keep their position without resorting to substantial public aid or government ownership.[28]

France, traditionally a high-subsidy country, annually pays about 400,000,000 francs under its system of contract services and, in addition, regularly guarantees extensive indebtedness of the contractors.[29] Operators other than contractors receive a navigation bounty of about 95,000,000 francs yearly, and have been eligible for low-interest construction loans totaling 1,500,000,000 francs in the last nine fiscal years.[30] To alleviate the acute depression in French shipping and shipbuilding in 1936, Parliament set aside 120,000,000 francs for additional domestic shipbuilding credit,[31] and distributed an extraordinary navigation bounty of 60,000,000 francs to contractors and 50,000,000 francs to other shipowners.[32] All regular forms of aid to the French merchant marine are based on fixed rates rather than a varying differential.

Nazi Germany has taken a strong stand against the "artificial maintenance of competing fleets by political measures,"[33] and has sought to obviate subsidies in Germany by breaking up the great shipping combines into small, scientifically managed units closely supervised by the government.[34] Substantial assistance has nevertheless been given to German operators in recent years. A credit of 70,000,000 marks was extended jointly to the Hamburg-America and North German Lloyd lines and one of 7,000,000 marks to tramp operators, for debt refinancing purposes; and outright subsidies of 20,000,000 marks and 8,700,000 marks have been provided, at fixed rates, for assistance in navigation and construction, respectively.[35]

Britain, from 1935 to 1937, departed from its general policy of limiting its shipping aid to the guarantee of shipbuilding loans.[36] For these three years it made available £2,000,000 annually to supplement the revenues of British tramp operators[37] and sponsored minimum rate agreements among all competitors in many routes[38] in an effort to lift world freight rates to pre-depres-

26. I.e., "any person or concern performing or supplying stevedoring, ship-repair, ship-chandler, towboat, or kindred services."

27. This prohibition may be modified or waived by four Commissioners.

28. During 1935 and 1936 even the Netherlands extended non-interest-bearing credits totaling 14,000,000 guilders to Dutch operators to equalize operating cost differentials. *Foreign Shipping News*, April 2, 1937. For an earlier survey of shipping aid, cf. deWilde, "Ship Subsidies and the Future of World Shipping," cited.

29. "American Ships in Foreign Trade," memorandum prepared by Jesse E. Saugstad, Bureau of Foreign and Domestic Commerce, Department of Commerce, 1935, printed in *Senate Document No. 224*, 74th Congress, 2nd Session, pp. 4ff. It is interesting to note that the government in the year 1935 alone guaranteed bond issues amounting roughly to 1,200,000,000 francs for companies operating on the Far Eastern and South American routes.

30. *Ibid.*, pp. 8-11; *Foreign Shipping News*, September 18, 1936.

31. *Foreign Shipping News*, December 18, 1936.

32. *Ibid.*, September 18, 1936.

33. German Institute for Business Research, *ibid.* October 9, 1936.

34. *Ibid.*, October 9, 1936, January 22 and 29, 1937; "American Ships in Foreign Trade," cited, pp. 13ff.

35. *Ibid.*, pp. 15-19.

36. Under the Trade Facilities Acts of Great Britain (1921-1926) and the Loans Guarantee Acts of Northern Ireland (effective 1922 to date), a grand total of £42,646,052 had been made available to September 30, 1934. *Ibid.*, pp. 29ff. The most recent guarantees under the Northern Ireland Acts are those announced in May 1937, totaling £2,467,000. *Foreign Shipping News*, June 11, 1937.

37. Part I of the *British Shipping (Assistance) Act, 1935* provided the following scale for annual tramp subsidies, based on movements in the freight rate index (1929=100):

Index	*Subsidies*	*Index*	*Subsidies*	*Index*	*Subsidies*
100	£ none	97	£ 750,000	94	£1,500,000
99	£250,000	96	£1,000,000	93	£1,750,000
98	£500,000	95	£1,250,000	92	£2,000,000

This program in its original form was effective for the year 1935 only. "American Ships in Foreign Trade," cited, pp. 26-28. For extensions through 1936 and 1937, cf. *Foreign Shipping News*, November 20, 1936 (supplement) and February 19, 1937.

38. *Fourth Report of the Tramp Shipping Administrative Committee*, reproduced in digest form in *Foreign Shipping News*, March 5, 1937. Cf. also, *ibid.*, October 23, 1936 and February 12, 1937.

sion levels. The result has been a marked improvement in the position of British shipping and a steadying of world rates.[39] During the two years ended in February 1937, Britain also provided a special fund of £10,000,000 for cargo-ship construction loans at 3 per cent, on condition that two tons of obsolete vessels be scrapped for every ton built.[40] Results have been disappointing, largely because of difficulties in meeting the scrapping requirement.[41] In connection with the merger of Cunard and White Star in 1934, the government extended mortgage loans totaling £11,000,000; of this sum £4,750,000 was used for the completion of the *Queen Mary*, £4,750,000 is being employed in the construction of the sister-ship ("Number 552"), and £1,500,000 went to the merger company as additional working capital.[42] To meet increased competition in the Pacific, particularly by the United States, the governments of Britain, Australia, New Zealand and Canada now propose to construct two liners, together costing between £2,500,000 and £2,800,000, and to provide a subsidy for their operation in the Vancouver-San Francisco-Australia-New Zealand trade.[43]

Italy's ship-aid program, which embraces contract-payments, construction subsidies, bounties for the scrapping of tonnage in Italy, and operating subsidies for cargo-ship operators not holding contracts, has not been altered materially since 1934. The merchant fleet itself, however, has been aligned more closely with the country's nationalist trade policies through a complete financial and administrative reorganization of shipping companies, begun in 1926 and completed early in 1937.[44]

Japan now pays about ¥9,500,000 annually for its contract services.[45] Under its scrap-and-build programs of 1932 and 1935 and its current building program, annual construction subsidies will have averaged roughly ¥3,300,000 over the fiscal years 1933-1940.[46] Tramp navigation subsidies have not been granted extensively heretofore, but an average annual sum of about ¥2,600,000 will be used for this purpose in the next four years.[47] All of these forms of outright subsidy are based on predetermined rates. Additional assistance is regularly available to Japanese operators in the form of credit at low interest rates. The close interrelation of government and industry in Japan gives rise to still further aids to shipping and shipbuilding, such as the substantial subsidy to the steel industry.[48]

A GOVERNMENT-OWNED MERCHANT MARINE?

Will the 1936 Act be more successful than previous legislation in securing the maintenance and rejuvenation of our merchant shipping? In its recent survey,[49] the Maritime Commission was unable to supply a conclusive answer. Under the leadership of chairman Joseph P. Kennedy, the Commission has set energetically about its task. It has negotiated adjustments with most of the companies holding the old mail contracts, and pending the development of a long-term program, it has accorded to seventeen lines six-month operating subsidies, recently renewed, involving the payment of $10,400,000 a year. The Commission has also tentatively outlined some twenty-three shipping services which would cover the major foreign trade requirements of the United States. It has decided against the advisability of developing tramp shipping and has termed the construction of large, fast ocean liners of the *Queen Mary* type undesirable for the United States.[50]

After surveying the prospects of new building, the Commission reluctantly concluded that "the disparity between the replacement requirements of the American merchant marine and probable con-

39. *Ibid.*

40. Part II of the "Assistance Act." "American Ships in Foreign Trade," cited, pp. 26ff.

41. Fifty vessels of 186,000 gross tons, costing £3,664,360, were built and 97 vessels of 386,625 gross tons were scrapped. Loans from the fund totaled only £3,548,124.7s.9d. Many applicants did not own "suitable tonnage" for scrapping under the law and found such vessels scarce and expensive in the open market. This difficulty is partly explained by the fact that "the Committee freely exercised their discretion in refusing to accept for demolition tonnage which in their opinion was too old to be really competitive." *Report of the Ships Replacement Committee, 15th March, 1937*, reproduced in *Foreign Shipping News*, June 25, 1937 (supplement).

42. *Foreign Shipping News*, April 16, 1937; "American Ships in Foreign Trade," cited, p. 24.

43. *Foreign Shipping News*, September 11 and December 31, 1936, May 7 and June 25, 1937; *Journal of Commerce*, May 24, 1937.

44. For details of the reorganization program, cf. *Foreign Shipping News*, January 15, 1937; also "American Ships in Foreign Trade," cited, pp. 37ff.

45. *Foreign Shipping News*, July 24, 1936, February 5 and June 4, 1937.

46. For details of the Ship Improvement Laws of 1932 and 1935, cf. "American Vessels in Foreign Trade," cited, p. 56. For the long-range construction aid program incorporated in the 1937-1938 subsidy bill enacted by the Diet in April, 1937, cf. *Foreign Shipping News*, June 4, 1937. Cf. *ibid.*, September 18, October 30, November 27, 1936; February 5, 1937. The significant fact about these three building programs from the standpoint of policy is that the first required a 2 to 1 ratio of scrapped tonnage to new tonnage; the second, a ratio of only 1 to 1; and the third abandoned the scrapping requirement altogether.

47. *Foreign Shipping News*, June 4, 1937.

48. "American Ships in Foreign Trade," cited, p. 61.

49. Cf. *Economic Survey of the American Merchant Marine*, cited.

50. In advising against the construction of super-liners, the Commission expressed the conviction that the development of transoceanic air services would impair the usefulness of fast express ships. *Ibid.*, p. 23.

struction is so great as to present a discouraging prospect for the industry as a whole."[51] To replace all ships which will be 20 years old and over by 1942 would require the construction of 1,305 vessels, aggregating 7,402,000 gross tons, at a total cost of $2,500,000,000.[52] While the expenditure of such a vast sum would obviously be impossible and the replacement of all ships would probably be undesirable as well, even a modest building program is by no means assured. Under the old mail contract system, 258 vessels totaling about 1,770,000 tons were subsidized. At present only nine of the subsidized lines, operating 111 ships with a gross tonnage of 774,842, are certain to survive and be eligible for subsidies. Of these companies, six have given the Commission contingent assurances that they will build 60 vessels in the next five years; and another line may construct five additional ships. This building would entail a total cost of $137,000,000, of which the government would probably contribute more than $50,000,000 in subsidies. Moreover, the program will be carried out only if the initial or down payment which the shipping companies must make is reduced from the present requirement of 25 per cent of the American cost to 25 per cent of the foreign cost. The same companies have also stipulated a minimum construction subsidy of 40 per cent and "satisfactory" operating subsidies.[53] The Commission admits that even if the required down payment is revised, there will still be no certainty that a substantial number of ships will actually be built by private concerns. There is only one definite commitment to build, namely a passenger vessel for the United States Lines. The Commission is trying to complete a program for the construction of 10 to 12 high-speed tankers in 1938 as part of a five-year plan for 40 such vessels. In the interest of national defense, the government is to pay the cost of increasing the speed beyond commercial requirements, but otherwise tankers are not entitled to subsidies under the law. In addition, 10 or 12 vessels may be built to replace obsolete ships in the government's own fleet.

The main obstacle to an extensive private shipbuilding program lies in the inadequate capital resources of American shipping companies. Few if any companies possess sufficient funds to finance construction without substantial sums of new capital. The Maritime Commission recognizes, however, that the public is reluctant to invest in an industry so completely dependent for its profits on continued government support over a long period of time. Our ship-aid policy has never been very stable, as was evidenced when the 1936 Act abrogated the 20-year mail subsidy contracts after they had been in effect only a few years. If profits are made in shipping, there is usually an immediate outcry against excessive subsidies and a threat of Congressional action. Moreover, government assistance "entails some measure of government control, which in turn means inflexibility, curtailment of investment, reduced earning power and, finally, an increased need for subsidies."[54] Ship-owners are always haunted by the fear of public ownership and operation, and they are not reassured by the 1936 Act, which calls for a merchant marine "owned and operated . . . by citizens of the United States *in so far as may be practicable.*"[55]

In order to encourage private investment and enterprise in shipping, the Maritime Commission has recommended a number of changes in the existing legislation:

1. Provision of specified protection for the shipping contractor in case of cancellation of subsidies without just cause or of default in subsidy payments. In such an event the contractor would have the right to demand that the government make good the default, or else buy back the subsidized ships at cost, less 5 per cent annual depreciation. If the government should fail to adopt either alternative, the operator would be entitled to transfer his ships to foreign registry after payment of all indebtedness secured by them.
2. Reduction of the down payment requirement from 25 per cent of the American costs of construction to 25 per cent of the foreign costs, since foreigners are never called upon to make a larger initial payment.
3. Permission to have ships constructed abroad whenever foreign costs are less than half American costs, and additional authorization enabling the Commission to allow foreign building whenever costs abroad are between 33⅓ and 50 per cent lower and bids from American yards are deemed "unreasonable and excessive."
4. Alteration of the provision which requires ship-owners to return to the government at five-year intervals one-half of the net profits in excess of 10 per cent. The Commission would permit the recapture of profits only after 10-year periods, in order to enable shipping companies to build up reserves for "lean" years.
5. Enlargement of the Commission's discretion to permit American ship companies to have affiliations with foreign-flag services and engage in such ancillary operations as the Commission may find

51. *Ibid.*, p. 43.
52. *Ibid.*, p. 38.
53. *Ibid.*, p. 40.
54. *Ibid.*, p. 1.
55. *Merchant Marine Act, 1936*, Section 101. Italics are the author's.

beneficial in the development of strong shipping services.

6. Authorization for the Commission to waive the insistence on $25,000 maximum salaries for shipping executives in order to attract better managerial talent.

While the Commission hopes the adoption of these amendments by Congress[56] will stimulate private investment in shipping, it is apparently convinced that the bulk of our merchant marine will have to be replaced by the government. In its opinion the crux of the problem is this:

"Many of our operators built their business on vessels which they secured from the government at prices as low as $5 a dead-weight ton. Who is going to replace these vessels at $200 a ton? The Commission is forced to conclude that, from all present indications, it will have to be the government."[57]

THE LABOR PROBLEM

The Commission warns that all government efforts to build up a strong merchant marine will be futile so long as nothing is done to end "deplorable" labor conditions, "to increase the efficiency of our crews and to restore order and discipline upon our ships."[58] During the last few years American shipping has been repeatedly paralyzed by labor conflicts, caused largely by strife between unions affiliated respectively with the American Federation of Labor and the Committee for Industrial Organization. In an effort to create some sort of order out of chaos, the Labor Relations Board has been holding elections among the ship employees of numerous companies to determine the proper bargaining agencies. In the opinion of the Maritime Commission, responsibility for the prevailing unsatisfactory labor relations must be ascribed in part to the employer who "has in the past imposed long hours, low wages and cramped quarters," and in part to the employee who "has abused his employment in a manner that would not be tolerated in any other industry."[59] Some alleviation of genuine grievances has been provided. The Seamen's Act of 1915 and the Copeland Personnel Act of 1936 have given seamen a high degree of immunity from arbitrary treatment, a standard 8-hour day and protection in case of sickness and death; and the six conventions dealing with these and related seamen's problems, which were passed by the International Labor Conference in the fall of 1936,[60] should benefit American seamen by establishing uniform high standards in all merchant fleets. Little has been done, on the other hand, to insure the efficiency and loyalty of crews. As a step in this direction, the Maritime Commission has now proposed the establishment of a tribunal for mediation in marine labor disputes, similar to that created in the railway field by the Railway Labor Act.[61] To attract and train a high type of seamen it is also providing courses of instruction for unlicensed personnel.

THE COST

If the Commission's efforts to rebuild and maintain the American merchant marine are successful, they seem certain to entail the expenditure of more public funds than have been spent under the laws of 1920 and 1928. Many factors prevent exact determination of the outlay required. The difficulty of calculating differentials in operating and construction costs[62] will give the Commission wide discretion in determining the size of the subsidy. Moreover, it will be difficult to estimate the amount that will ultimately be needed until the Commission's program is fully developed. At present the temporary operating subsidies granted to seventeen shipping lines total about $10,000,000 a year, but the Commission estimates that actually $15,000,000 to $20,000,000 will be necessary to give American ships full parity with foreign lines. The modest building program for 65 ships outlined by the Commission will require an annual government contribution of $10,000,000 for the next five years. Thus the total construction and operating subsidies would provisionally aggregate from $25,000,000 to $30,000,000 a year, as compared with a mail subsidy of $24,637,224 paid in the fiscal year 1936. If private companies prove unable to finance construction of all or part of the 65 ships now projected, the government must contribute still more. Nor should it be forgotten that this program will cover only a small part of the replacement needs of the merchant fleet. If a substantial portion of over-age vessels are to be replaced in the next decade, the American public must be prepared to spend many more millions on American shipping. It remains to be seen

56. To give effect to the Commission's recommendations, Senator Copeland has introduced into the second session of the 75th Congress *A Bill to Amend the Merchant Marine Act of 1936, and for Other Purposes.*

57. *Economic Survey of the American Merchant Marine,* cited, p. 43.

58. *Ibid.*

59. *Ibid.*, p. 44.

60. *International Labour Review,* November 1936. Cf. also U.S. Department of Labor, *Monthly Labor Review,* May 1936.

61. *Economic Survey of the American Merchant Marine,* cited, p. 48.

62. On this point, cf. Jesse E. Saugstad, "The Problem of Differential Subsidies," *Pacific Marine Review,* November 1936; also *Economic Survey of the American Merchant Marine,* cited, pp. 70-75.

whether all the necessary appropriations will be made by Congress.

Would this expenditure be justified? Congress apparently believes so now, and the Maritime Commission has tried to prove the point. An efficient American merchant marine is thought necessary to promote and safeguard the foreign commerce of the United States. It is argued that only the establishment and maintenance of a network of American lines can provide the direct, speedy and reliable service to foreign markets which American farmers, industrialists and merchants require. To rely heavily on foreign ships for the transportation of our goods might risk serious interruptions of service in emergencies, especially in case of foreign war when other countries would withdraw their ships for the fulfillment of national needs. It is by no means certain, however, that even the existence of a considerable American merchant fleet would preclude a shortage of shipping facilities during wars involving the major maritime powers whose vessels normally carry a large portion of this country's commerce. Moreover, at such a time, American ships might be debarred by the Neutrality Act of 1937 from carrying many of our exportable goods to their normal destinations. Yet an American-flag fleet capable of carrying a "substantial portion" of our regular trade would offer the only available insurance against such a dire lack of tonnage as that which gave rise to the Shipping Act of 1916, and the only promising means of discovering emergency markets for goods ordinarily consumed by belligerent nations.

The most important justification of a strong merchant marine is its value to national defense. In time of war combination passenger and cargo vessels could be converted into aircraft carriers, auxiliary cruisers and hospital ships. Freighters could be used to supply the navy and armed forces fighting overseas; and fast tankers would be needed to fuel our cruisers, battleships and destroyers. At the same time we would require many vessels to bring in essential raw materials and take out the goods necessary to pay for them. The Navy Department has estimated that the military and naval forces of the country would require a minimum of 1,000 merchant ships, aggregating 6,000,000 gross tons, in the early stages of any war with a major power.[63] Since the American merchant fleet at present includes only 1,400 sea-going vessels of 2,000 gross tons and over, totaling 8,407,000 gross tons, this national defense program would clearly entail the mobilization of almost our entire tonnage. Unless many vessels in excess of ordinary commercial requirements were built and laid up at great expense for the eventuality of war, only a relatively small number of ships would remain free to carry the imports and exports which during war would probably surpass peace time volume. Even the complete replacement of the existing American fleet with modern commercial vessels equipped for auxiliary service might therefore fall short of serving fully the combined needs of our national defense and our commerce. But it is a statistical fact that such rehabilitation would place this country in a stronger position at sea than any other power except Britain, and would make another $3,000,000,000 shipbuilding orgy unnecessary.

The charge is frequently made that the Merchant Marine Act of 1936 is characteristic of the nationalist efforts of almost all maritime countries to foster shipping. While the Act seeks only to equalize foreign and domestic construction and operation costs, it might, if unwisely administered, stimulate a building race with other nations. Since it authorizes the Maritime Commission to offset foreign subsidies with additional aid, the subsidy burden would become progressively heavier if other countries took counter-measures. Nationalist competition might lead once more to serious over-tonnaging of the world's fleets, with resulting declines in freight rates and depression in the shipping industry. While the world's tonnage at the end of 1936 was 3,000,000 gross tons less than in 1929, the total rose for the first time last year and has continued to increase in 1937. Regardless of the effects of American policy, governments may in the end find it desirable to broach an international agreement for the reciprocal reduction of shipping aid. At present, however, such a development appears remote.

Meanwhile, some satisfaction may be found in the fact that a frank and direct approach to the subsidy problem has at last been attempted and that the most exhaustive examination of the conditions and needs of the American merchant marine in the country's history has been made. Taxpayers have been told as nearly as possible what a first-class merchant fleet will cost. If they, through Congress, confirm their purpose of developing such a fleet, they seem to be assured of more intelligent planning and more businesslike administration than in the past two decades.

63. *Economic Survey of the American Merchant Marine*, cited, p. 10.